

BEFORE THE STATE BOARD OF EQUALIZATION
OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of }
M. B. SHEFTALL }

Appearances:

For Appellant: Harry Kahan, Certified Public
 Accountant

For Respondent: Burl D. Lack, Chief Counsel:
 Crawford H. Thomas, Associate
 Tax Counsel

O P I N I O N

This appeal is made pursuant to Section 18593 of the Revenue and Taxation Code from the action of the Franchise Tax Board on the protest of M. B. Sheftall to a proposed assessment of additional personal income tax in the amount of \$680.81 for the year 1946.

The proposed additional assessment arose because of the inclusion by the Franchise Tax Board in gain realized from the sale or exchange of capital assets amounts debited to Appellant's account on the books of a corporation to which he had transferred an interest in a mining lease. The notice of the additional assessment was issued more than four years, but less than six years, after Appellant's return was filed. The Appellant contends that the amounts debited to his account did not represent income and that he made full disclosure of the transaction in his return, and, hence, that the proposed assessment is barred by the statute of limitations.

In 1945 Appellant acquired a one-fourth interest in a mining lease on property in the State of Nevada. In 1946 he and the other lessees assigned the lease to the American Silver Corporation, a Nevada corporation. At the same time Appellant and his fellow assignors purchased a large number of shares in the corporation at a nominal price. For the purpose of developing the mining lease it was the intention of the corporate management to raise working capital by assessing its shares, all of which were assessable. As consideration for the assignment of the lease Appellant, with the other assignors, was to receive payment of an agreed amount, at a specified percentage of the proceeds received by the corporation from the extraction

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and sale of ore. The assignment agreement also provided that any assessment levied upon the shares of stock held by the assignors would be offset against the consideration to be paid them for assigning the lease.

During the year 1946 three assessments were levied in the aggregate amount of 15 cents per share, which amounted to \$16,755.00 upon Appellant's shares. This amount was debited by the corporation to amounts due or to become due under the assignment. A corresponding amount was credited against his liability for the stock assessments.

The difference between the amount of the assessments against his shares of stock and the basis of Appellant's interest in the mining lease was not set forth in his tax return as a capital gain or otherwise as income. Instead, Appellant attached to the return a statement in which he described the foregoing transaction in detail and in which he claimed that the debiting of assessments to his account on the books of the corporation did not constitute the realization of income. No valuable ore deposits were discovered by the corporation and it made no sales of ore.

Section 18586.1 of the Revenue and Taxation Code as it read at the time the notice of proposed additional assessment was given provided:

"If the taxpayer omits from gross income an amount properly includible therein which is in excess of 25 percent of the amount of gross income stated in the return, the tax may be assessed at any time within six years after the return was filed."

Otherwise the normal limitation period is four years as provided in Section 18586 of the Code,

We are aware of no court decisions which have construed Section 18586.1 of the Revenue and Taxation Code. Section 275(c) of the Internal Revenue Code, which prior to 1954 read substantially the same as Section 18586.1, and which provided for a five year limitation in omission cases has, however, been provocative of much litigation and there are many cases which have construed its provisions. These cases indicate that there has been much confusion in the application of the word "omit" in Section 275(c). See Ketcham v. Commissioner of Internal Revenue, 142 Fed. 2d 996; Reis v. Commissioner of Internal Revenue, 142 Fed. 2d 900; M. C. Parrish and Co. v. Commissioner of Internal Revenue, 19, aff'd. 147 Fed. 2d 284; O'Bryan v. Commissioner of Internal Revenue, 148 Fed. 2d 456; Estate of C. P. Hale v. Commissioner of Internal Revenue, 1 T.C. 121.

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The more recent decisions, however, have departed from the rationale of the earlier cases and have adopted a uniformly liberal interpretation of the statute. (Uptegrove Lumber Co. v. Commissioner of Internal Revenue, 204 Fed. 2d 570; Deakman-Wells Co., Inc. v. Commissioner of Internal Revenue, 213 Fed. 2d 894; Slaff v. Commissioner of Internal Revenue, 220 Fed. 2d 65; Davis v. Hightower 230 Fed. 2d 549.) Under these cases the test is not whether a specific item of income has been entered on the right line in the return but rather whether it has been completely omitted. Thus in the Deakman-Wells decision the court pointed out that it is not expected that the form supplied by the Commissioner can always be followed, and that the longer period of limitations is not applicable "if all items of gross income are disclosed in a schedule attached to the return in which the computation is made." On the basis of these decisions we are of the opinion that Section 18586.1 of the Revenue and Taxation Code did not operate to extend the period within which the Franchise Tax Board could issue an assessment against Appellant.

Since we have concluded that the assessment was barred by the statute of limitations, it will not be necessary to consider Appellant's contention that he realized no income on the transaction included in the assessment,

O R D E R

Pursuant to the views expressed in the Opinion of the Board on file in this proceeding, and good cause appearing therefor,

IT IS HEREBY ORDERED, ADJUDGED AND DECREED, pursuant to Section 18595 of the Revenue and Taxation Code, that the action of the Franchise Tax Board on the protest of M.B. Sheftall to a proposed assessment of additional personal income tax in the amount of \$680.81 for the year 1946 be and the same is hereby reversed.

Done at Sacramento, California, this 21st day of November, 1957, By the State Board of Equalization.

Robert E. McDavid, Chairman

J. H. Quinn, Member

Geo. R. Reilly, Member

Paul R. Leake, Member

Robert C. Kirkwood, Member

ATTEST: Dixwell L. Pierce, Secretary